No. 82-914

IN THE
Supreme Court of the United States
OCTOBER TERM, 1982

MONSANTO COMPANY,
Petitioner,
v.

SPRAY-RITE SERVICE CORPORATION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF AMICUS CURIAE OF NATIONAL AGRICULTURAL CHEMICALS ASSOCIATION IN SUPPORT OF REVERSAL

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BRIEF AMICUS CURIAE OF NATIONAL AGRICULTURAL CHEMICALS ASSOCIATION IN SUPPORT OF REVERSAL[1]

INTEREST OF AMICUS CURIAE

The National Agricultural Chemicals Association ("NACA") is a non-profit membership corporation organized under the laws of the state of Delaware to further the interests of its members. Practically all of the major domestic producers and formulators of pesticides and herbicides—including Petitioner Monsanto Company—are NACA members. Together, NACA's 105 member companies produce or formulate roughly 90% of the pesticides (including herbicides) used in this country.

The central issue in this case is the extent to which manufacturers of agricultural chemicals and other prod-

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[1] This brief is filed with the consent of the parties pursuant to Supreme Court Rule 36.2. The written consents have been filed with the Clerk of the Court.

ucts may safely employ pro-competitive, non-price vertical restrictions in distributing their products. NACA member companies will be directly and substantially affected by the Court's resolution of this issue.

Many NACA member companies sell their agricultural chemical products through independent distributors. Together, these NACA members account for a preponderance of the agricultural chemicals that are sold in this fashion domestically. Many NACA manufacturing members share Monsanto Company's interest in competing vigorously by ensuring an acceptable level of effort from its distributors. All value their freedom to fashion effective distribution programs without unreasonable antitrust exposure. Accordingly, NACA has a vital interest in submitting a brief to the Court addressing the legal issues raised by this case, without, however, addressing the factual disputes between the parties.

SUMMARY OF ARGUMENT

The basic problem posed in this case is the need to give reality to this Court's ruling in *GTE Sylvania* that vertical non-price restrictions may have pro-competitive justifications that render them lawful under the "rule of reason." [2] If vertical *price* agreements remain subject to the traditional rule of *per se* illegality, the Court will have to consider other approaches to protecting the integrity of *GTE Sylvania* and the ability of manufacturers safely to employ pro-competitive, non-price vertical restrictions. The reason, which is discussed further below, is straightforward: if "price" agreements are too broadly defined or too readily found, *GTE Sylvania* is thoroughly undermined.

In Section I of this brief we sketch some of the real-life business circumstances that should shape this Court's effort to harmonize rule-of-reason treatment of non-price

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[2] *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 54, 58 (1977).

vertical restrictions with *per se* prohibition of resale price-fixing. In the context of restricted distribution systems validated by *GTE Sylvania*, these circumstances include the inevitability, and indeed desirability, of frequent communication between the manufacturer and its distributors about all matters of concern, including prices, and the fact that the manufacturer's implementation of non-price restrictions will inevitably affect distributors' ability to engage in intrabrand price competition.

Section II of the brief deals principally with the appropriate standards of proof that should be met by a price-cutting distributor claiming that his termination by the manufacturer was "pursuant to a conspiracy with other distributors to fix the resale price" of the product. (Pet. A-17.) Here we show that if *GTE Sylvania* is to have practical reality, the distributor should not recover unless he offers convincing evidence (i) excluding the possibility that the manufacturer, in terminating the distributor, was enforcing reasonable non-price restrictions and (ii) establishing that other distributors were in fact adhering to minimum resale prices because of agreements or threats of termination.

In Section III we assume that vertical "price" agreements have been properly proved, and we discuss the kinds of agreements that should be excluded from the scope of the *per se* rule if *GTE Sylvania* is not to be undermined. We conclude that the *per se* rule should not apply to price or price-affecting agreements that are intrinsic or reasonably ancillary to valid non-price restrictions. We also discuss the danger to *GTE Sylvania* from too readily finding an unlawful "vertical-horizontal" conspiracy from collective actions by distributors connected with a manufacturer's enforcement of distributional restraints. Finally, we note that reasonable non-price restraints should not be rendered illegal *per se* by the presence in the same distribution system of unlawful resale price maintenance agreements.

ARGUMENT

I. The Economic Realities of Restricted Distribution Should Guide This Court's Effort To Harmonize the Principles of *GTE Sylvania* with the Traditional *Per Se* Rule Against Resale Price Maintenance.

In legal theory, a manufacturer could institute and operate a restricted, or "franchised," distribution system without any communication to or from its distributors or franchisees, existing or prospective, concerning the operation of the distribution system. In practice, this cannot be expected to happen, and for perfectly legitimate reasons. Maximizing efficiency in distribution, like rational economic planning in general, depends on the manufacturer's maintaining a flow of the best available market information, of which distributors are an important source. Efficient distribution is a cooperative enterprise, and it is not only inevitable, but affirmatively desirable, that there be communication between a manufacturer and its distributors, and that they exchange views on the common problems arising from the operation of the distribution system.

Some of those common problems will almost certainly relate to the pricing of the products involved. As this Court recognized in *GTE Sylvania*, intrabrand price effects are intrinsic to non-price vertical restraints. When a manufacturer elects to limit the number of distributors to whom he will sell, or to impose territorial or customer restrictions on the distributors, he directly limits the number of intrabrand competitors to whom any particular buyer can turn. Similarly, manufacturer-imposed requirements that distributors perform promotional and other services necessarily lead to nominally higher prices to consumers by imposing higher costs on distributors. Such limitations on intrabrand competition and consequent price effects make it possible to achieve the distribu-

tional efficiencies and the level of distributor-supplied services that the manufacturer can legitimately seek. As Judge Posner has observed, "[t]he adoption of a restricted distribution system implies a decision to emphasize non-price competition over price competition, which such a system tends to suppress." [3]

A related and highly relevant point is that a distributor who disregards non-price restrictions, or a would-be distributor denied supplies by resale restrictions on franchised distributors, will often be a price discounter. The distributor who sells outside his assigned territory, and/or fails to provide promotional or other services desired by the manufacturer, will normally have to undercut the price charged by other distributors; buyers have no reason to pay the same price to a distant, less convenient seller or to one not providing services that its competitors supply. In short, disregard of non-price restrictions or obligations will commonly be accompanied by discounting.

Finally, the manufacturer's hostility toward the non-performing (and price-cutting) distributor will naturally be shared by affected distributors who are abiding by the manufacturer's non-price restrictions or obligations. It should hardly be surprising if distributors complain, and legitimately, about the price-cutting distributor who invades their territories; who sells to unfranchised distributors who in turn heavily discount the resale price; or who they have reason to believe, because of the depth of the price-cutting, is "free-riding" and not providing the costly services that they supply at the manufacturer's behest. And, of course, the fact of price-cutting will not go unmentioned.

As the instant case and others have shown, these economic realities of restricted distribution systems raise the danger that the manufacturer legitimately seeking to

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[3] *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 743-44 (7th Cir. 1982).

implement pro-competitive non-price restrictions will be held to have participated in an unlawful conspiracy to fix the distributors' resale prices. The principal antitrust pitfalls are as follows:

(1) Termination of a price-cutting distributor following complaints by competitors may be held sufficient, as in the instant case (Pet. A-5 - A-9), to establish that the termination was the product of an agreement or "concerted action" between the manufacturer and the complainants.

(2) The same facts may be held sufficient, as in the instant case (Pet. A-14 - A-17), to establish that the manufacturer and the complaining distributors were engaged in a *per se* unlawful conspiracy to maintain resale prices.

(3) Refusal of the manufacturer and other distributors to supply the terminated distributor may be characterized, again as in the instant case (Pet. A-9 - A-11, A-18), as a *per se* illegal "boycott."

(4) Communication among distributors before or during complaints to the manufacturer may be held to establish an unlawful "horizontal" agreement, to which the manufacturer becomes a party by terminating the offender.[4]

The protection provided by *GTE Sylvania* to the non-price restraints inherent in restricted distribution systems is undermined, if not eradicated, by legal risks of this sort. The result is to inhibit employment of efficient distribution systems benefitting manufacturers and consumers alike. Harmonization of the traditional prohibition of resale price maintenance with *GTE Sylvania* requires both (1) more careful rules as to the standard of proof of vertical price "agreement" under Section 1, and (2) more precise delineation of the kinds of vertical "price" agreements that fall within the traditional *per se* rule.

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[4] See the discussion in III-B, *infra*, of *United States v. General Motors Corp.*, 384 U.S. 127 (1966).

II. The Court Below Misunderstood the Appropriate Standard of Proof of Vertical Price Agreements To Be Applied in the Context of a Restricted Distribution System.

The court below seriously undermined the principles of *GTE Sylvania* by treating evidence of distributor complaints about price-cutting followed by termination as sufficient to establish an agreement to terminate for price-cutting, and by holding that proof that a manufacturer terminated a distributor because he was a price-cutter was sufficient to establish a resale price-fixing conspiracy between the manufacturer and other distributors. In this section of our brief we deal with these two errors in turn.

A. Termination of a Price-Cutting Distributor Following Complaints About the Price-Cutting Does Not Establish an Agreement To Terminate for Price-Cutting.

Contrary to the view of the court below (Pet. A-15), proof that one or more distributors in a restricted distribution system complained to the manufacturer about the price-cutting activities of another distributor, followed by the manufacturer's termination of that distributor, is plainly *not* sufficient to establish that the termination was the result of, or pursuant to, an agreement or "concerted action" between the manufacturer and the complaining distributors.

There is no such agreement where the manufacturer terminates a distributor for his own independent reasons, and the fact that the termination followed complaints does not prove that such independent reasons were lacking. To assume a causal link between complaints and subsequent termination is to commit the *post hoc, propter hoc* fallacy—the rooster's notion that the sun comes up because he crows before dawn. The complaints may simply be the source of information, which, had the manu-

facturer obtained it in other ways, would have led to the same result. Where that is the case, it makes no difference what the manufacturer's reason is, whether it be the failure of the dealer to engage in desired promotional activities, to abide by non-price restrictions, or to refrain from price-cutting activities.[5] Whatever bearing termination for price-cutting may have on whether an unlawful resale price maintenance scheme exists (*see* II-B and III-A-3 below), the mere fact that termination follows complaints does not prove that the manufacturer agreed with complainants to take such action.

Even if a termination may be said to reflect an "agreement" with other distributors, proof that the terminated dealer was a substantial price-cutter and that termination followed complaints does not demonstrate that the agreement was a "price-fixing" agreement or conspiracy. Suppose that a manufacturer, in imposing legitimate servicing and promotional obligations on his distributors, has explicitly assured them that he will terminate any distributor who fails to comply. It is perfectly reasonable for the distributors to ask for such assurance, as they could not both provide the required services and meet the prices charged by one who does not, and thus it is perfectly reasonable for the manufacturer to give it. That the defaulting distributor who is terminated was also a price-cutter does not convert the "agreement" into a "price-fixing" agreement.[6]

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[5] Nor does proof that complaining distributors have communicated among themselves before or during the course of making their complaints support an inference that the subsequent termination reflected agreement between them and the manufacturer. The complaints may still be nothing more than a source of information that would have led to termination in any event.

[6] Moreover, contrary to the court below (Pet. A-9 n.4), such an agreement cannot, consistently with *GTE Sylvania*, be characterized as a *per se* unlawful concerted refusal to deal. *See* III-A-1, *infra*. Whether an "agreement" to terminate for price-cutting is sufficient to invoke the *per se* rule is further explored in III-A-3 and III-B, *infra*.

In any event, since disregard of non-price restrictions and substantial discounting commonly go together, and since distributors can properly complain to the manufacturer about what they believe to be free-riders' violations of non-price obligations or restrictions, it is clear that *GTE Sylvania*'s protection of legitimate non-price restraints becomes an illusion if a terminated distributor can establish an unlawful conspiracy merely by proving that the termination followed other distributors' complaints about his price-cutting. Such proof establishes neither the reason for termination nor that the termination was the product of agreement. A manufacturer, after all, has no control over the wording of its distributors' communications to it or among themselves, nor can it be expected that they will complain, and the manufacturer will terminate, without mention or thought of price.

Thus, if we are to protect the manufacturers' right to pursue such a legitimate distribution system, proof of an agreement to terminate for price-cutting must consist of more than facts that might commonly occur within that distribution scheme. At the least, a plaintiff seeking to show that his termination was the result of an unlawful conspiracy to eliminate price competition must negate the alternative hypothesis—at least equally likely—that the manufacturer was following a policy of enforcing non-price obligations. The minimum proof on this point required of the plaintiff distributor should be solid evidence that either (1) the plaintiff was in full compliance with the non-price restrictions imposed on him and therefore the complaints about his discounting furnish the only apparent explanation for his termination, or (2) although plaintiff was not in compliance with all non-price restrictions, the manufacturer knowingly did not terminate other non-price-cutting distributors who similarly failed to comply and, again, the complaints about his discounting are the only apparent reason for the manufacturer's decision to terminate him. Any lighter burden

of proof would undermine *GTE Sylvania* by subjecting the manufacturer to unacceptable risks in attempting to operate a lawful system of restricted distribution.[7]

B. Proof that a Manufacturer Terminated a Distributor Because He Was a Price-Cutter About Whom Other Distributors Complained Does Not Establish a Conspiracy To Eliminate or Reduce Resale Price Competition.

The holding of this court in *United States v. Colgate*, 250 U.S. 300 (1919) must, as an irreducible minimum, mean that the unilateral action of a manufacturer in terminating a distributor is not covered by Section 1 of the Sherman Act, regardless of his reasons. By definition, there is no agreement between the manufacturer and the distributor terminated for price-cutting—termination reflects lack of agreement. Accordingly, absent proof of horizontal agreement among distributors on resale price, to establish the element of agreement there must be proof of vertical agreements between the manufacturer and the other, complaining distributors.

[7] Even in cases alleging horizontal agreements, where communications among competitors are properly viewed with suspicion, plaintiffs must show more than "consciously parallel" actions plus the opportunity (at trade association meetings or otherwise) to collude. Since parallel actions may be consistent with independent decisions that each competitor would have made regardless of what the others did, plaintiffs must adduce evidence showing that they were consistent with individual self-interest only if all acted the same way. *E.g., Proctor v. State Farm Mutual Automobile Insurance Co.,* 675 F.2d 308, 334 (D.C. Cir.), *cert. denied,* 103 S. Ct. 86 (1982); *Michelman v. Clark-Schwebel Fiber Glass Corp.,* 534 F.2d 1036 (2d Cir.), *cert. denied,* 429 U.S. 885 (1976); *Venzie Corp. v. United States Mineral Products Co.,* 521 F.2d 1309, 1313 (3d Cir. 1975). The case is even stronger for requiring a terminated distributor claiming a vertical price-fixing conspiracy to show more than that competitors complained to the manufacturer of his price-cutting. As we have pointed out, communications between a manufacturer and his distributors are a valuable source of information necessary to the implementation of legitimate non-price restraints.

Adequate proof that *one* distributor was terminated for price-cutting and not for failure to adhere to non-price restraints, while it is of course evidence of the manufacturer's concern with resale prices, does not by itself establish agreement by *other* distributors that they will abide a price floor. In order to make out such agreements, there should be, at a minimum, proof (1) that the manufacturer communicated to its other distributors its desire that they sell at suggested minimum resale prices (or that they not sell below some specific discount); (2) that the manufacturer explicitly or by strong implication threatened them with termination (perhaps by holding up the example of the terminated distributor) if they did not follow his desires; *and* (3) that many if not most did adhere to the minimum resale prices desired by the manufacturer.

In this connection, Monsanto's Petition for Certiorari states as follows:

> With rare exceptions, respondent and all other Monsanto distributors sold below—often substantially below—Monsanto's suggested resale prices. . . . One of respondent's witnesses testified that 'price cutting was a way of life with distributors.' . . . It is undisputed that no distributor ever changed its resale prices as a result of any alleged pressure by Monsanto, . . . despite contradicted evidence that Monsanto threatened respondent and one other distributor with termination. (Pet. at 6-7.)

If this is a correct summary of the record, there were no resale price maintenance agreements proved in the instant case even if Spray-Rite had been terminated "because" it was a price-cutter and not because of its failure to satisfy Monsanto's non-price distributorship criteria.

Nor does proof that other distributors complained to the manufacturer about the terminated distributor's price-

cutting supply the necessary additional evidence. Superficially considered, these complaints might be thought to suggest that the other distributors have been parties to a resale price maintenance scheme. But that is not the only or even the most likely inference where a system of restricted distribution is involved. The other distributors' complaints may merely indicate their distress over a competitor charging prices lower than they, who are dutifully supplying costly services, can profitably charge, and their request that the manufacturer do something about it. There is no reason to hold, or even suggest, that such complaints alone make them parties to an unlawful conspiracy.

III. Vertical "Price" Agreements Intrinsic or Reasonably Ancillary to Valid Non-Price Restrictions Should Be Excluded from the Rule of *Per Se* Illegality, As Should "Vertical-Horizontal" Price-Affecting Agreements Arising in the Course of a Manufacturer's Operation of a Valid Restricted Distribution System.

The threat posed to *GTE Sylvania* by this and similar cases cannot be adequately resolved solely by rules regarding the proof necessary to establish conspiracy or agreement. A limited distribution system by its nature rests on a web of agreeemnts, and actions taken pursuant to them will inescapably have price effects. Consequently, the more critical task is to determine, in light of *GTE Sylvania*, what kinds of "resale price agreements" are or are not to be deemed illegal *per se*. In addressing this issue, it may be useful to begin with some general observations concerning *per se* rules.

Strictly speaking, a rule of *per se* illegality means that an agreement is illegal without more. No other facts need be proved or considered. No proof is required of market power or of actual market effects, and no justifications

will be accepted. As this Court has often said, the severity of such a rule dictates that it be adopted only when the economic support for it is clear.[8] Thus, even in the area of horizontal agreements, the *per se* rule does not apply to all agreements with price effects.

For example, agreements to disseminate price and other market information through trade associations or other organized channels are not *per se* illegal, despite the fact that such dissemination—by providing information not otherwise available—inevitably affects the prices charged by individual sellers or paid by individual buyers. The reason is plain: dissemination of information, as in an organized stock exchange, may improve the competitive performance of the market.[9] Agreed-upon dissemination of price information becomes unlawful only when an analysis of market structure, other market facts, and the details of the information disclosed, indicates that reduction of price competition is the likely effect.[10]

Even a "horizontal" agreement on price may be lawful if reasonably ancillary to a lawful joint venture, such as a joint venture formed by competitors to enable them to enter another market that they individually could not efficiently reach.[11] And in its recent *BMI* decision, this Court held that an agreement among competitors on the price to

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[8] *E.g., GTE Sylvania*, 433 U.S. at 49-50; *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 19-20 (1979).

[9] *Maple Flooring Manufacturers Ass'n v. United States*, 268 U.S. 563, 582-83 (1925).

[10] *E.g., United States v. Container Corp. of America*, 393 U.S. 333 (1969); *American Column & Lumber Co. v. United States*, 257 U.S. 377 (1921).

[11] The ancillarity principle was set forth as early as *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 280 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

be charged for a collective product offering does not invoke the *per se* rule. The Court prefaced its analysis with the following comments:

> . . . "[P]rice-fixing" is a shorthand way of describing certain categories of business behavior to which the *per se* rule has been held applicable . . . . [A] literal approach does not alone establish that . . . [a] particular practice is one of those types. . . . *Thus, it is necessary to characterize the challenged conduct as falling within or without that category of behavior to which we apply the label "per se price-fixing."* [12]

Care in limiting the scope of the *per se* rule on vertical resale price-fixing is *a fortiori* required. In holding that territorial and customer restrictions on distributors are to be treated under the rule of reason, the Court in *GTE Sylvania* recognized that vertical restrictions are inherently less productive of anticompetitive effects than horizontal agreements. In so doing, the Court completely eliminated one half of the parallel to horizontal restraints, for horizontal agreements among competitors to divide territories or to allocate customers, like horizontal price-fixing agreements, are illegal *per se*.[13] The same more favorable regard for vertical restrictions, even if it is not taken to compel the conclusion that all vertical price-fixing should be treated under the rule of reason (433 U.S. at 51 n.18), at least suggests that the kinds of vertical "price" agreements subject to a *per se* rule should be very carefully defined.

Following that approach, we now turn to the kind of agreements "fixing" or otherwise affecting resale price that are properly excluded from the scope of the *per se* rule.

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[12] *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 9 (1979) (emphasis added).

[13] *E.g., White Motor Co. v. United States*, 372 U.S. 253, 263 (1963).

A. The Rule of Reason Should Apply to Agreements Involving Price Effects That Are Intrinsic or Reasonably Ancillary to Non-Price Restrictions.

1. *Agreements with price effects intrinsic to non-price restraints.* As recognized in *GTE Sylvania*, price effects are intrinsic to various non-price restrictions and to actions taken to implement or enforce them. The inevitable effect of many non-price restrictions is to reduce the number of distributors of a product to whom particular buyers may turn. Termination of the price-cutting distributor who has failed to abide by non-price restrictions or obligations necessarily raises the price to buyers who have patronized him, at least in the short run. Agreements preventing wholesalers from selling to other than franchised retailers, and agreements preventing franchised retailers from selling to other than consumers, inevitably keep the manufacturer's product from getting into the hands of likely discounters.[14] *GTE Sylvania* clearly requires that all such agreements, in which price effects are indirect but intrinsic, be exempted from the rule of *per se* illegality.

In this connection, while petitioner has not raised the issue here, we believe it to be appropriate for the Court to repudiate the ruling below that an agreement among a manufacturer and remaining distributors to refuse to supply product to a terminated dealer is a *per se* illegal boycott. Respondent, in its brief in opposition to the petition for certiorari, makes much of this holding, using it to buttress its claim that a price-fixing conspiracy among the manufacturer and its distributors had in fact occurred. But proof of a "concerted refusal to deal" with a terminated distributor adds nothing to an understanding of

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[14] Similarly, the manufacturer who elects to deal only with "prestige" retail outlets, on the understanding that conversion to a "discount"-type of operation will lead to termination, has created a distribution system in which higher prices will be charged than would otherwise be the case.

why the manufacturer terminated the distributor or what, if any, agreements there may have been between the manufacturer and other distributors with respect to resale prices.

As we have noted, an agreement by distributors with the manufacturer that they will not sell to unauthorized outlets is intrinsic to a limited distribution system. If such agreements were forbidden as "boycotts," a manufacturer could create a limited distribution system only by vertical integration. For many products, and for many small manufacturers, vertical integration is not feasible; and even where it is, it would make no sense to force a manufacturer to go that route when in his judgment independent distributors could do the job more efficiently.[15] Similarly, if agreements by distributors not to deal with parties not authorized to participate in the distribution system were taken as evidence of other, unlawful agreements, restricted distribution systems would be saddled with unwarranted legal risks.

2. *Price agreements clearly ancillary to non-price restrictions.* As noted above, it is a familiar proposition that an agreement that would be unlawful standing alone (a "naked" restraint) may be lawful if ancillary to some other valid business arrangement. Without attempting to canvass all of the possibilities, we furnish two examples of agreements directly dealing with resale price that are clearly ancillary to non-price restrictions and should accordingly be treated under the rule of reason.

The first example is found in *Eastern Scientific*, where the First Circuit upheld, against a claim of *per se* illegality, a contractual restriction preventing dealers from selling outside their defined territories at less than a minimum price specified by the manufacturer.[16] The court

[15] *Compare GTE Sylvania*, 433 U.S. at 56 n.25, and at 57 n.26.

[16] *Eastern Scientific Co. v. Wild Heerbrugg Instruments, Inc.*, 572 F.2d 883, 886 (1st Cir.), *cert. denied*, 439 U.S. 833 (1978).

reasoned that this restriction could not have a greater anticompetitive effect than an absolute territorial limitation, and that it was therefore lawful if the latter would pass muster. The result could also have been justified on another ground, namely that the "minimum price" provision in fact served as a maximum price check, because any distributor who charged above that price would lose sales to distributors from adjacent territories. In other words, it enabled the manufacturer to achieve the efficiencies and other legitimate purposes derivable from territorial limitations, and at the same time prevent territorially protected distributors from abusing their position by charging too high a price.

The second, and related, example of clearly ancillary vertical price agreements is a manufacturer's restriction on the maximum resale prices charged by distributors participating in a system of restricted distribution. This example leads, of course, to the proposition that *Albrecht v. Herald Co.*, 390 U.S. 145 (1968), extending the rule of *per se* illegality to vertical maximum resale price maintenance, should be expressly overruled.[17] The ban on maximum resale price maintenance impedes a manufacturer's ability to implement, with full advantage to consumers, the kind of beneficial non-price restrictions which *GTE Sylvania* endeavored to protect.

Albrecht itself was a classic example. Exclusive distribution of newspapers has obvious cost savings; it is highly inefficient to have two or more distributors driving trucks and sending newsboys over the same streets. But if the only paper in town grants exclusive territorial distribution rights, the distributor will in all likelihood take advantage of its position by charging a high resale price, to the disadvantage of the newspaper, which thereby loses

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[17] The Court may have taken a step in this direction in *Arizona v. Maricopa County Medical Society*, 457 U.S. 332, 102 S. Ct. 2466, 2475 n.18 (1982), when it noted in discussing *Albrecht* and *Kiefer-Stewart* that "horizontal restraints are generally less defensible than vertical restraints."

sales, and of the consumers, who pay more than they would pay with a markup closer to distribution cost. Maximum resale price maintenance enables the publisher to achieve the efficiencies of exclusive distribution and at the same time insure that the cost savings will be passed on to consumers.[18]

3. *Price agreements reasonably ancillary to maintaining an effective distribution system.* We turn now to a more difficult case that comes closer to the core of the *per se* rule against minimum resale price maintenance. A manufacturer may determine that a limited distribution system is necessary to facilitate the provision of services and other forms of non-price competition that will make it a more effective interbrand competitor. At the same time, it determines that within each wholesale or retail territory, it is best served by having a substantial number of distributors, both to provide locational convenience for all buyers and to have sufficient price competition to keep the distributors on their toes. In other words, it would not elect to set absolute minimum resale prices even if the law permitted it to do so. Nevertheless, it remains legitimately concerned that resale prices not fall to the point that the bulk of its distributors could not profitably handle its product and still provide the services that it desires. Accordingly, its concern with resale prices charged by particular distributors appears reasonably ancillary to the implementation of non-price restrictions and obligations that may be lawful under *GTE Sylvania*.

As we have earlier pointed out, the *per se* price-fixing rule is not implicated if a terminated distributor was failing to provide the required services. Nor is it implicated

[18] *Albrecht* can be read as not foreclosing the defense of "ancillarity" set forth above. In *Albrecht* the Court declined to accept the publisher's claim that its maximum price-fixing conduct was necessary because the publisher had failed to offer evidence of the existence of exclusive territories, their reasonableness, or the economic power over price they placed in the hands of the distributors. 390 U.S. at 153.

by the termination itself, which is accurately characterized as the manufacturer's unilateral response to the market facts confronting it. The problem arises if the manufacturer's actions lead to an understanding by the distributors that excessive price discounting must be avoided, as it then may be plausibly argued that there are vertical agreements to abide by some resale price floor, distinct or indistinct.

A good case can be made for the proposition that a manufacturer should be permitted to offer the facts set forth above as a defense to a claim of *per se* illegal resale price maintenance. The case is narrow in scope and effect. It can arise only where there is provable jeopardy to a distribution system; it involves selective circumstances particularized to a manufacturer's specific distribution system and goals and the ability of its distributors to perform services; and any flash point of the manufacturer's pricing concern will likely be well below the pricing point the distributors would choose through a horizontal cartel. Such a limited concern with resale pricing is of course much less restrictive of intrabrand or interbrand competition than rigid enforcement of the manufacturer's specified minimum resale price (or, indeed, of a system of closed, exclusive territories that might be upheld under the rule of reason). And in terms of ancillarity, it is arguably no more restrictive than is necessary to meet the legitimate objectives that *GTE Sylvania* viewed with favor.

Moreover, such actions do not raise one of the principal dangers posed by minimum resale price maintenance, namely that it may be employed by manufacturers in a concentrated industry as a device to facilitate the suppression of price competition among the manufacturers themselves.[19] Adherence to a horizontal price stabilization

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[19] *See, e.g.*, "Resale Price Maintenance—Antitrust Division View," 5 Trade Reg. Rep. (CCH) ¶ 50,442 at 56,013 (August 17, 1982) (Letter from Assistant Attorney General Baxter to Congressman McClory).

scheme depends heavily on the ability of the competing manufacturers to detect each other's price cuts. If detection is difficult or long-delayed, firms with excess capacity are strongly tempted to make a secret price-cut, as it will generate substantial additional sales before the competitors realize what has happened. If, on the other hand, detection is quick, the manufacturer who makes the cut cannot hope to gain from it because it will be immediately matched. Distribution through independent distributors complicates the detection problem. Without manufacturer-specified resale prices, competing manufacturers cannot know whether a distributors' price cut on one manufacturer's product was made on the distributor's own initiative or was the result of a secret discount on the manufacturer's price to him. Where, however, each manufacturer specifies his distributors' resale price, a price cut by one manufacturer can be readily identified. In short, limited intervention in resale pricing, leaving a substantial degree of distributor pricing freedom, does not serve the anticompetitive purpose of facilitating reduction of price competition at the manufacturers' level.

We recognize that the suggested distinction is not without problems. There may be close cases where the line is difficult to draw. On the other hand, it should be fairly readily determinable, in the probably few cases where the issue would need to be reached, whether or not there has been active competition on resale prices. In any event, this Court's prior decisions do not appear to have foreclosed the question. The Court's decisions dealing directly with vertical resale price maintenance have been cases in which the manufacturer, by contract or by coercion, has endeavored to compel distributors strictly to abide by minimum resale prices set by it.[20]

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[20] *Dr. Miles Medical Co. v. John D. Park & Sons*, 220 U.S. 373 (1911); *United States v. Schrader's Son*, 252 U.S. 85 (1920); *FTC v. Beech-Nut Packing Co.*, 257 U.S. 441 (1922); *Ethyl Gasoline Corp. v. United States*, 309 U.S. 436 (1940); *United States v. Univis Lens Co.*, 316 U.S. 241 (1942); *United States v. Park, Davis*

B. "Vertical-Horizontal" Agreements That Affect Price Should Be Assessed Under the Rule of Reason When They Arise Out of the Operation of a Lawful System of Restricted Distribution.

Even if, as urged in Section III-A above, it were made clear that the protection of *GTE Sylvania* extends to vertical "price" agreements inherent in or ancillary to lawful non-price distributional restraints, that protection would be undermined if a finding of "vertical-horizontal" conspiracy were allowed too readily to lead to *per se* condemnation of otherwise legitimate vertical restraints. The dangers are graphically illustrated by *United States v. General Motors Corp.*, 384 U.S. 127 (1966), where the collective efforts of GM and its franchised Los Angeles dealers to stop sale of cars by the dealers to or through non-franchised "discounters" was found to be a *per se* unlawful "combination or conspiracy."

The result might have been rested on the ground—hinted at in the opinion—that the company's efforts to stop the practice were attributable to concerted pressure by the dealers, not its own business determination that the restrictions would serve its interest in efficient procompetitive distribution. This Court so characterized the rationale when in *GTE Sylvania* it described the *GM* case as involving "restrictions originating in agreements among the retailers." (433 U.S. at 58 n.28.)

The opinion in *General Motors*, however, goes much further. The following passages are particularly pertinent:

> General Motors sought to elicit from all the dealers agreements, substantially interrelated and interde-

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& Co., 362 U.S. 29 (1960). Less than rigid resale price-maintenance may have been involved at the retailing level in *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944), but the illegality of the resale term (obligating retailers to "maintain prevailing local price schedules") was conceded on appeal and therefore not before the Court. 321 U.S. at 715, 719.

pendent, that none of them would do business with the discounters. These agreements were hammered out in meetings between non-conforming dealers and officials of General Motors' Chevrolet Division, and in telephone conversations with other dealers. It was acknowledged from the beginning that substantial unanimity would be essential if the agreements were to be forthcoming. And once the agreements were secured, General Motors both solicited and employed the assistance of its alleged co-conspirators in helping to police them. . . . This process for achieving and enforcing the desired objective can by no stretch of the imagination be described as "unilateral" or merely "parallel."

* * *

Elimination, by joint collaborative action, of discounters from access to the market is a *per se* violation of the Act. . . . [W]here businessmen . . . deprive others of access to merchandise which the latter wish to sell to the public, we need not inquire into the economic motivation underlying their conduct.

* * *

We note, moreover, that inherent in the success of the combination in this case was a substantial restraint upon price competition—a goal unlawful *per se* when sought to be effected by combination or conspiracy. . . . And the *per se* rule applies even when the effect upon prices is indirect.

* * *

[I]t is conceded that General Motors is intensely concerned that each of its dealers has an adequate "profit opportunity", a concern which necessarily involves consideration of the price realized by dealers.[21]

Absent proof that imposition of such resale restrictions was coercively extracted from a reluctant manufacturer by conspiratorial distributor pressure—which in the case of General Motors seems rather unlikely—these proposi-

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[21] *United States v. General Motors Corp.*, 384 U.S. at 144-45, 146, 147, 148 n.23 (1966).

tions cannot co-exist with the basic principles established by *GTE Sylvania.* It should make no difference to the applicability of a rule of reason to non-price restrictions that: (1) a problem has been called to the attention of the manufacturer by a concerted presentation of distributor complaints; (2) joint collaborative action has excluded discounters from access to the market; (3) a substantial restraint on price competition is inherent in the action taken by the manufacturer; or (4) the manufacturer is concerned that its distributors have an adequate profit opportunity. Nor should it make any difference that the manufacturer has solicited and obtained the assistance of its distributors in helping to police its restrictions. If the restrictions are a legitimate pro-competitive device, there is no reason why the manufacturer should be compelled to set up its own monitoring system when the use of its distributors, who are on the scene, will generate the information more quickly and cheaply.[22]

C. Reasonable Non-Price Distributional Restraints Are Not Rendered Illegal *Per Se* by the Presence of Unlawful Resale Price Maintenance Agreements.

Finally, it is worth pointing out that even in a case where it is proved that the manufacturer was a party to unlawful resale price maintenance agreements, it makes no sense, after *GTE Sylvania,* to hold that otherwise lawful non-price restrictions are thereby rendered illegal *per se.* The fact, if it is a fact, that a manufacturer has superimposed unlawful resale price agreements on non-price restrictions that are themselves pro-competitive does not mean that the latter have lost their beneficial character. Accordingly, a distributor who is terminated for failure

[22] As the foregoing discussion should indicate, we are not proposing that the Court abandon the distinction between vertical and horizontal restraints expressed in *GTE Sylvania.* We do not suggest immunity for distributor cartels that coerce manufacturers into adopting distributional restraints—price or non-price—that in the latter's judgment would disserve their and the consumers' interest in efficient and competitively-priced product-service offerings.

to fulfill service obligations, or for selling outside his assigned territory at discounted prices, cannot recover simply by proving that the manufacturer also required distributors to adhere to specified minimum resale prices. Instead, the jury should be instructed in such cases that it must evaluate the restrictions under the rule of reason. This Court's decisions do not require any different result.[23]

CONCLUSION

This Court should reverse the judgment of the court below and clarify the relationship between *GTE Sylvania*'s rule of reason treatment of vertical non-price restrictions and the traditional rule of *per se* illegality for resale price maintenance agreements.

Respectfully submitted,

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[23] *United States v. Sealy, Inc.*, 388 U.S. 350 (1967), relied on by the court below, is readily distinguishable as the territorial restraints were expressly stated to be horizontal, not vertical. In fact it was unnecessary for the Court, once having found the restraints to be horizontal, to have struck them down on the ground they were related to price-fixing, because horizontal territorial agreements are unlawful in and of themselves.